

BEFORE THE TENNESSEE REGULATORY AUTHORITY AT

NASHVILLE, TENNESSEE

January 10, 2005

IN RE:

**PETITION OF APPALACHIAN POWER COMPANY
FOR FINANCING UP TO \$950,000,000 THROUGH
DECEMBER 31, 2005**

**DOCKET NO.
04-00371**

ORDER APPROVING FINANCING TRANSACTIONS

This matter came before Chairman Pat Miller, Director Deborah Taylor Tate and Director Sara Kyle of the Tennessee Regulatory Authority (the "Authority" or "TRA"), the voting panel assigned to this docket, at the regularly scheduled Authority Conference held on January 10, 2005 for consideration of the *Application of Appalachian Power Company* ("Application") for authorization, pursuant to Tenn. Code Ann. § 65-4-109 (2004), to issue, sell, and deliver secured and unsecured promissory notes in the aggregate principal amount of up to \$950,000,000.

Statutory Framework

Tenn. Code Ann. § 65-4-109 (2004) provides:

No public utility shall issue any stocks, stock certificates, bonds, debentures, or other evidences of indebtedness payable in more than one (1) year from the date thereof, until it shall have first obtained authority from the [TRA] for such proposed issue. It shall be the duty of the [TRA] after hearing to approve any such proposed issue maturing more than one (1) year from the date thereof upon being satisfied that the proposed issue, sale and delivery is to be made in accordance with law and the purpose of such be approved by the [TRA].

Background

Appalachian Power Company ("Appalachian") is a Virginia corporation with its principal offices located in Roanoke, Virginia. Although the majority of Appalachian's customers are located in Virginia, Appalachian is qualified to transact business in Tennessee and provides power to Kingsport Power Company.

The Virginia State Corporation Commission approved the proposed transactions, subject to certain limitations and requirements, by an order dated November 30, 2004 in Case No. PUE-2004-00123 ("Virginia Order"). The Virginia Order is attached hereto as Exhibit 1 and incorporated by this reference as a part of this *Order Approving Financing Transactions*.

Application

In its *Application*, filed with the TRA on October 22, 2004, Appalachian requests approval from the TRA to issue and sell, from time to time through December 31, 2005, secured and unsecured promissory notes ("Notes") in the aggregate principal amount up to \$950,000,000. The Notes may be issued in the form of either (1) First Mortgage Bonds, to be secured by Appalachian's Mortgage and Deed of Trust, as amended and supplemented by one or more new Supplemental Indentures, or (2) senior notes or other unsecured promissory notes pursuant to Indentures and company orders. Appalachian filed exhibits with its *Application* showing the general form of the proposed Notes and associated documents.

Appalachian also seeks approval to issue up to \$200,000,000 out of the \$950,000,000 aggregate principal of the Notes to its parent company, American Electric Power Company, Inc. ("AEP"), through one or more unsecured notes. In the *Application*, Appalachian affirmed that the interest rates on any Notes issued to AEP would parallel AEP's cost of capital, in accordance with the Public Utility Holding Company Act of 1935, as amended. In addition, Appalachian

will sell Notes to AEP only if the effective cost of the Notes is lower than or equal to the effective cost of an unsecured Note of similar terms and conditions sold to non-affiliated entities.

In association with these transactions, Appalachian plans to utilize interest rate management techniques and to enter into Interest Rate Management Agreements (“IRMAs”). The TRA previously authorized Appalachian’s use of these methods,¹ and Appalachian requests that the TRA continue the authorization through December 2005. According to the *Application*, the aggregate notional amount of Appalachian’s outstanding IRMAs will not exceed twenty-five percent of Appalachian’s existing debt obligations.

Use of Proceeds and Compliance with Regulations

Appalachian states that it will use the proceeds from issuance of the Notes (1) to redeem, directly or indirectly, long-term debt, (2) to refund, directly or indirectly, preferred stock, (3) to repay short-term debt at or prior to maturity, (4) to reimburse Appalachian’s treasury for construction program expenditures; and (5) for other proper corporate purposes. Appalachian further asserts that it will complete the transactions in compliance with all applicable indenture, charter, and other standards relating to debt and equity securities and capitalization ratios of Appalachian.

January 10, 2005 Authority Conference

At the January 10, 2005 Authority Conference, the Directors voted unanimously to approve the *Application*, upon a finding that the proposed transaction will be made for a proper purpose and in accordance with Tennessee laws.

¹ See *In re Appalachian Power Company (American Electric Power) \$450,000,000 Application For Financing For Year 2004*, Docket No. 03-00503, *Order Approving Financing Transactions* (February 6, 2004)

IT IS THEREFORE ORDERED THAT:

1. Appalachian Power Company is authorized to issue and sell up to \$950,000,000 of Notes, from time to time during the period January 1, 2005 through December 31, 2005, for the purposes and under the terms and conditions set forth in its *Application*.

2. This authorization is subject to the limitations and requirements set forth in ordering paragraphs numbered one through ten of the Virginia Order, which is attached as Exhibit 1.

3. The authorization and approval given hereby shall not be used by any party, including, but not limited to, any lending party, for the purpose of inferring an analysis or assessment of the risk involved to a purchaser of any Appalachian Notes or securities. Nothing contained herein creates or is intended to create any liability on the part of the Tennessee Regulatory Authority, the State of Tennessee, or any political subdivision thereof for the transaction approved herein.

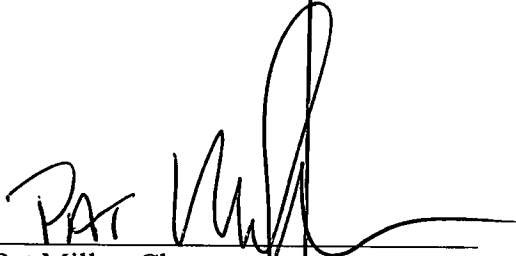
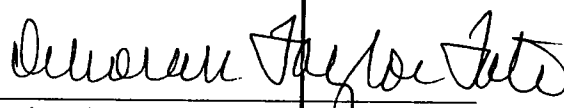
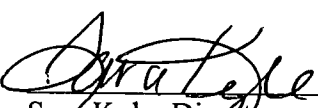

Pat Miller, Chairman
Deborah Taylor Tate, Director
Sara Kyle, Director

Exhibit 1

Virginia State Corporation Commission
Case No. PUE-2004-00123
Order dated November 30, 2004

COMMONWEALTH OF VIRGINIA
STATE CORPORATION COMMISSION

AT RICHMOND, NOVEMBER 30, 2004

APPLICATION OF

APPALACHIAN POWER COMPANY

CASE NO. PUE-2004-00123

For authority to incur
long-term debtORDER GRANTING AUTHORITY

On October 21, 2004, Appalachian Power Company ("APCO", or "Applicant") filed an application with the Virginia State Corporation Commission ("Commission") under Chapters 3 and 4 of Title 56 of the Code of Virginia for authority to issue long-term debt to the public and to an affiliate. In conjunction, Applicant requests authority to enter one or more interest rate hedging arrangements to protect against future interest rate movements in connection with the long-term debt securities to be issued. Furthermore, APCO requests authority to utilize interest rate management techniques by entering into various Interest Rate Management Agreements ("IRMAs"). Applicant has paid the requisite fee of \$250.

APCO proposes to issue secured or unsecured promissory notes ("Notes") up to the aggregate principal amount of \$950,000,000 from time to time through December 31, 2005. The Notes may be issued in the form of First Mortgage Bonds, Senior Notes, or other unsecured promissory notes. Within certain limitations, APCO requests flexibility to select specific terms and conditions for the Notes based on market conditions at the time of issuance. The Notes will have maturities of not less than 9 months and not more than 50 years. The interest rate may be fixed or variable. The fixed rate of any note shall not exceed by more than 350 basis points the yield to maturity on United States Treasury obligations of comparable maturity at the time of pricing of the Notes. The initial interest rate on any variable rate Note will not exceed 10% per annum.

APCO requests authority to issue up to \$200,000,000 out of the \$950,000,000 aggregate principal amount of Notes to its parent company, American Electric Power Company, Inc. ("AEP"), through one or more unsecured Notes. APCO states that the interest rates on any Notes issued to AEP would parallel AEP's cost of capital in accordance with the Public Utility Holding Company Act of 1935, as amended ("PUHCA"). However, the Notes will only be sold to AEP if their effective cost is lower than or equal to the effective cost of an unsecured Note of similar terms and tenor sold to non-affiliated entities.

APCO intends to sell the Notes (i) by competitive bidding; (ii) through negotiation with underwriters or agents; (iii) by direct placement with a commercial bank or other institutional investor; or (iv) to its parent company, AEP. Issuance costs are expected to be less than 1.0% of the principal, with no costs incurred on Notes issued to AEP. The proceeds from the issuance of the Notes will be used to redeem, directly or indirectly, long-term debt; to refund, directly or indirectly, preferred stock; to repay short-term debt; to reimburse APCO's treasury for construction program expenditures; and for other proper corporate purposes. If it is found to be cost advantageous, proceeds from the issuance of the Notes may be used for the early redemption of up to \$45,000,000 of APCO's First Mortgage Bonds, 8.0% Series due 2025, which becomes eligible for early redemption at 1.04% of the principal amount on June 1, 2005.

In conjunction with the issuance of the proposed securities, Applicant requests authority, through December 31, 2005, to enter into one or more interest rate hedging arrangements to protect against future interest rate movements in connection with the issuance of the Notes. Such hedging arrangements may include, but not be limited to, treasury lock agreements, forward-starting interest rate swaps, treasury put options, or interest rate collar agreements ("Treasury Hedges"). All Treasury Hedges will correspond to one or more of the Notes. Consequently, the cumulative notional amount of the Treasury Hedges cannot exceed \$950,000,000.

Finally, APCO requests a continuation of the authority granted in Case No. PUE-2004-00003 to utilize interest rate management techniques and enter into IMRAs through December

31, 2005.¹ The IRMAs will consist of interest rate swaps, caps, collars, floors, options, hedging forwards or futures, or any similar products designed and used to manage and minimize interest costs. IRMA transactions will be for a fixed period and based on a stated principal amount that corresponds to an underlying fixed or variable rate obligation of APCO. APCO will only enter IRMAs with counterparties that are highly rated financial institutions. The aggregate notional amount of the IMRAs outstanding will not exceed 25% of APCO's existing debt obligations.

THE COMMISSION, upon consideration of the application and having been advised by its Staff, is of the opinion and finds that approval of the application will not be detrimental to the public interest. We will approve the application subject to the terms and conditions detailed herein.

Accordingly, IT IS ORDERED THAT:

(1) Applicant is hereby authorized to issue and sell up to \$950,000,000 of Notes, from time to time during the period January 1, 2005, through December 31, 2005, for the purposes and under the terms and conditions set forth in the application.

(2) Notes issued in accordance with Ordering Paragraph (1) for the purpose of refunding maturing debt are limited to the aggregate principal amount of \$500,000,000, while remaining Notes may be issued to increase outstanding debt or for the early redemption of existing debt, when it is cost effective and interest savings can be demonstrated.

(3) Applicant is hereby authorized to issue and sell up to \$200,000,000 of the total \$950,000,000 authorized in Ordering Paragraph (1) to AEP, provided that the effective cost of such Notes is lower than or equal to the effective cost of an unsecured Note of similar terms and conditions sold to non-affiliated entities.

(4) Applicant is authorized to enter into the hedging agreements for the purposes set forth in its application and to the extent that the aggregate notional amount outstanding does not to exceed \$950,000,000 during the period January 1, 2005 through December 31, 2005.

¹ Pursuant to the Commission's Order Granting Authority, dated February 11, 2004, in Case No. PUE-2004-00003, APCO's existing authority to utilize IRMAs is set to expire after December 31, 2004.

(5) Applicant is authorized to enter into IRMAs for the purposes set forth in its application and to the extent that the aggregate notional amount outstanding does not exceed 25% of Applicant's total outstanding debt obligations during the period January 1, 2005, through December 31, 2005.

(6) Applicant shall not enter into any IRMA or hedging transaction involving counterparties having credit ratings of less than investment grade.

(7) Applicant shall submit a preliminary Report of Action within ten (10) days after the issuance of any debt pursuant to this Order to include the type of debt, the issuance date, the amount of the issue, the interest rate, the maturity date, and any securities retired.

(8) Applicant shall submit a preliminary Report of Action within ten (10) days after it enters into any hedging agreement or IRMA pursuant to Ordering Paragraphs (4) and (5) to include: the beginning and, if established, ending dates of the agreement, the notional amount, the underlying securities on which the agreement is based, an explanation of the general terms of the agreement that explain how the payment obligation is determined and when it is payable, and a calculation of the cumulative notional amount of all outstanding IRMAs as a percent of total debt outstanding.

(9) Within 60 days after the end of each calendar quarter in which any debt is issued pursuant to this Order, Applicant shall file a more detailed Report of Action to include: the type of debt issued, the date and amount of each series, the interest rate, the maturity date, net proceeds to Applicant, an itemized list of expenses to date associated with each issue, a description of how the proceeds were used, a list of any securities retired with a corresponding analysis to demonstrate the cost savings associated with the refunding, a list of all hedging agreements and IRMAs associated the debt issued, and a balance sheet reflecting the actions taken.

(10) Applicant's Final Report of Action shall be due on or before March 1, 2006, to include the information required in Ordering Paragraph (9) in a cumulative summary of actions taken during the period authorized.

(11) The authority granted herein shall have no implications for ratemaking purposes.

(12) Approval of this application does not preclude the Commission from applying the provisions of § 56-78 and § 56-80 of the Code of Virginia hereafter.

(13) The Commission reserves the right to examine the books and records of any affiliate, whether or not such affiliate is regulated by this Commission, in connection with the authority granted herein, pursuant to §56-79 of the Code of Virginia.

(14) This matter shall remain under the continued review, audit, and appropriate action of this Commission.

AN ATTESTED COPY hereof shall be sent to Applicant, to the attention William E. Johnson, Attorney, American Electric Power, 1 Riverside Plaza, Columbus, OH, 43215-2372; and to the Commission's Division of Economics and Finance and Public Utility Accounting.